

Internal Revenue Service

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Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

Telephone Number:

Refer Reply To:

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PLR-127942-09

Date:

October 19, 2009

Legend

Taxpayer =

A =

Year 1 =

Date 1 =

Date 2 =

\$a =

\$b =

Dear

This is in response to your letter requesting permission to revoke an election made by A pursuant to §1.163(d)-1(c) of the Income Tax Regulations to treat qualified dividends and net capital gain income as investment income under §§ 163 (d)(1) and 163 (d)(4)(B) of the Internal Revenue Code for Year 1. A died on Date 1, and as executor of Taxpayer, you request permission to revoke A's election.

FACTS

For Year 1, A hired an accounting firm (Firm) to prepare his Form 1040, Individual Income Tax Return (return). The Firm prepared it by entering the relevant data into a tax software computer program (software program) during which a keying error was mistakenly made on line 4g of Form 4952 that resulted in an inadvertent election to include the entire amount of qualified dividend income and net capital gain of \$a as investment income for purposes of the deduction of the investment interest expense. The actual amount of investment interest expense was \$b, an amount significantly less than \$a.

After the Firm entered the return information in the software program, the Firm ran a final diagnostic error check on the return. The diagnostic check did not disclose any errors. After this, the Firm manually reviewed the return in accordance with the Firm's quality control policies and procedures. Because all of the investment interest expense of \$b was allowed on Form 4952, there was an oversight in discovering that an excessive election amount had been made on line 4g of Form 4952 which affected the tax calculation.

The error was discovered by another professional tax preparer engaged by Taxpayer to assist with the administration process. The Firm was contacted by the other professional tax preparer on Date 2 and was advised of the Form 4952 election.

After being contacted, the Firm reviewed its files and the Year 1 return. It discovered that the diagnostic error check, provided by the Firm's Year 1 tax software computer program, does not identify an excessive investment income election as a possible error for returns that are manually filed by paper. However, this possible error is identified if a return is filed electronically. The Firm was unaware of the differences in the computer tax software in identifying this type of error. Because the Taxpayer chose not to file electronically, the possible error was not identified in the return diagnostics.

APPLICABLE LAW

Section 163(d) provides that, in the case of a taxpayer, other than a corporation, the amount allowed as a deduction for investment interest shall not exceed the net investment income of the taxpayer for the taxable year.

Section 163(d)(4)(B) defines the term, "investment income," in general, as the sum of

- (i) gross income from property held for investment (other than gain taken into account under clause (ii)(I)),
- (ii) the excess (if any) of
 - (I) the net gain attributable to the disposition of property held for investment, over
 - (II) the net capital gain determined by only taking into account gains and losses from dispositions of property held for investment, plus
- (iii) so much of the net capital gain referred to in clause (ii)(II) (or if lesser, the net gain referred to in clause (ii)(I)) as the taxpayer elects to take into account under this clause.

Section 163(d)(4)(B) also states that the term shall include qualified dividend income (as defined in § (1)(h)(11)(B)) only to the extent the taxpayer elects to treat such income as investment income for purposes of this subsection.

Section 1.163(d)-1(b) provides that the elections for net capital gain and qualified dividend income under §163(d)(4)(B) must be made on or before the due date (including extensions) of the income tax return for the taxable year in which net capital gain is recognized or the qualified dividend income is received.

Section 1.163(d)-1(c) provides that the election under § 163(d)(4)(B) is revocable with the consent of the Commissioner.

The Taxpayer is requesting permission to revoke an election made by A to treat qualified dividends and net capital gain income as investment income. This situation is analogous to those situations concerning taxpayers who have not made a particular election provided in the regulations because of inadequate or incorrect advice from knowledgeable tax professionals and are subsequently seeking extensions of time under § 9100 of the Regulations on Procedure and Administration. See Rev. Rul. 83-74, 1983-1 C.B. 112.

Section 301.9100-3 generally provides extensions of time for making regulatory elections. For this purpose, § 301.9100-1(b) defines the term “regulatory election” to include an election whose due date is prescribed by a regulation, a revenue ruling, revenue procedure, notice or announcement published in the Internal Revenue Bulletin.

Section 301.9100-3 provides that requests for extensions of time for regulatory elections will be granted when the taxpayer provides evidence (including affidavits described in the regulations) to establish to the satisfaction of the Commissioner that the taxpayer acted reasonably and in good faith and granting relief will not prejudice the interests of the government.

Section 301.9100-3(b)(1) states that a taxpayer will be deemed to have acted reasonably and in good faith if the taxpayer-

- (i) requests relief before the failure to make the regulatory election is discovered by the Service;
- (ii) failed to make the election because of intervening events beyond the taxpayer's control;
- (iii) failed to make the election because, after exercising due diligence, the taxpayer was unaware of the necessity for the election;
- (iv) reasonably relied on the written advice of the Service; or

(v) reasonably relied on a qualified tax professional, and the tax professional failed to make, or advise the taxpayer to make, the election.

In this case, A may be considered to have acted reasonably and in good faith because A relied on the Firm, a qualified tax professional, to prepare the return. The Firm used a software program that made an erroneous election that was not discovered by the Firm despite its diligent efforts.

Under § 301.9100-3(b)(3), a taxpayer will not be considered to have acted reasonably and in good faith if the taxpayer—

(i) seeks to alter a return position for which an accuracy-related penalty has been or could be imposed under § 6662 at the time the taxpayer requests relief (taking into account any qualified amended return filed within the meaning of § 1.6664-2(c)(3)) and the new position requires a regulatory election for which relief is requested;

(ii) was informed in all material respects of the required election and related tax consequences, but chose not to file the election; or

(iii) uses hindsight in requesting relief. If specific facts have changed since the original deadline that make the election advantageous to a taxpayer, the Service will not ordinarily grant relief.

In this case, Taxpayer is not seeking to alter a return position for which an accuracy-related penalty has been or could be imposed under § 6662 at the time relief is requested. A was not informed in all material respects of the related tax consequences of making the election because A was unaware an election had been made. Furthermore, Taxpayer is not using hindsight in requesting relief. Specific facts have not changed since the filing of the return and making of the original election that made the election disadvantageous to the Taxpayer.

Section 301.9100-3(c)(1)(i) provides, in part, that the interests of the government are prejudiced if granting relief would result in the taxpayer having a lower tax liability in the aggregate for all taxable years affected by the election than the taxpayer would have had if the election had been timely made (taking into account the time value of money). Section 301.9100-3(c)(1)(ii) provides, in part, that the interests of the government are ordinarily prejudiced if the taxable year in which the regulatory election should have been timely made, are closed by the period of limitations on assessment. Under these criteria, the interests of the government are not prejudiced in this case. Allowing the revocation of the election would not result in a lower tax liability in the aggregate for all taxable years affected by the election than would have been the case if the election had been timely made (taking into account the time value of money).

Furthermore, the taxable year in which the regulatory election that is sought to be revoked here, and any taxable year affected by it, is not closed by the period of limitations on assessment.

In addition, granting the revocation in the present situation would not cause undue administrative burden, nor would it be inconsistent with the objectives of the underlying statute and the regulatory election.

Accordingly, the consent of the Commissioner is hereby granted to revoke the election under §163(d)(4)(B) to include \$a as investment income for Year 1.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, for any such return filed electronically, a statement must be attached to the return that provides the date and control number of the letter ruling. The ruling contained in this letter is based upon information and representations submitted by Taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party.

While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

JOHN P. MORIARTY
Chief, Branch 1
(Income Tax & Accounting)